Office of Chief Counsel
Internal Revenue Service

memorandum

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JJPosedel

date: JAN 20 1999

to: Steve Castaneda, Manager, Large Dollar Collection Group
Attn: Revenue Officer Pat Medina, Riverside POD

from: Associate District Counsel, San Diego
Southern California District

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subject: [redacted]

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You have requested this office's opinion as to the applicability of I.R.C. § 6503(h) under the following circumstances.

[redacted] was a California partnership engaged in the [redacted] business. [redacted] and [redacted] were the general partners. [redacted] commenced business in [redacted]. It accrued employment tax liabilities for many quarters, including the third quarter of [redacted]. The partnership filed a Chapter 11 petition on [redacted]. The partnership's plan of reorganization was confirmed on [redacted]. All of the partnership's pre-petition tax liabilities were paid through the plan except for its employment tax liability for the third quarter of [redacted]. The partnership defaulted on its plan payments to

the Internal Revenue Service and the United States Trustee filed a motion to dismiss the case. On [redacted], the Court granted the U.S. Trustee's motion. Neither [redacted] nor [redacted] filed a personal bankruptcy petition at any time relevant to this issue. You ask whether the partnership's bankruptcy extended the statute of limitations for collection of the employment liability for the third quarter of [redacted].

I.R.C. § 6502(a) affords the Internal Revenue Service 10 years to collect a "tax imposed by this title [Title 26]." Employment taxes are imposed by Title 26 (26 U.S.C. § 3403). I.R.C. § 6503(h) suspends the running of the statute of limitations for collection of a tax imposed by Title 26 " . . . in a [bankruptcy] case . . . for the period during which the Secretary is prohibited by reason of such case . . . from collecting and . . . for 6 months thereafter." Under Bankruptcy Code § 362(a)(6), the filing of a bankruptcy petition operates as a stay of "any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case . . . ." The liability of the partners for the employment tax in issue here is derivative from the liability of the partnership and arises due to the operation of state law (i.e., California Corporations Code § 15015(a)(2)). Livingston v. United States, 92-1 U.S.T.C. ¶ 50,137 (D. Ida. 1992). There is no independent basis under the Internal Revenue Code for the assessment against the individual partners of a partnership which owes an employment tax liability. See, Calvey v. United States, 448 F. 2d 177 (6th Cir. 1971). There is, accordingly, only one statute of limitations which can be affected by I.R.C. § 6503(h) and that is the statute for collection from the taxpayer partnership.

Thus, we believe that the statute of limitations for collection of the employment tax liability was extended for the period the automatic stay was in effect with respect to [redacted], and for six months thereafter. See, United States v. Wright, 57 F. 3d 561 (7th Cir. 1995). This does not end the inquiry, however.

Bankruptcy Code § 362(c)(2)(C) provides that the automatic stay is in effect in a Chapter 11 case until a discharge is granted or denied. Recall that the partnership's Chapter 11 plan of reorganization was confirmed on [redacted]. Bankruptcy Code § 1141(d)(1) provides, in part, that "[e]xcept as otherwise provided in this subsection, in the plan, or in the order confirming the plan, the confirmation of a plan --(A) discharges [a non-individual] debtor from any debt that arose before the date of such confirmation . . . ." Were this debtor an individual, Bankruptcy Code § 1141(d)(2) would operate so as to prevent a discharge of any debt nondischargeable under Bankruptcy Code § 523.

Further, the plan or order confirming the plan does not, in the language of § 1141(d)(1), otherwise provide; in fact, the order confirming the plan states that the debtor is "discharged from any debt that arose prior to the hearing on confirmation, whether or not a proof of claim based upon such debt was filed." It is for this precise reason that the language of any proposed plan or order confirming a plan should be scrutinized carefully.

What effect did the dismissal of the case some three and one half years after the plan's confirmation have on this issue? Bankruptcy Code § 349 deals with a dismissal's effect. Subsection (b)(1) of § 349 provides for the reinstatement of any custodianship under § 543, any transfer avoided under specific Bankruptcy Code sections, and any lien voided under § 506(d). Subsection (b)(2) provides that an order of dismissal vacates any order, judgment or transfer ordered under other specific Bankruptcy Code sections. The legislative history to § 349 states that the basic purpose of the section is to undo the bankruptcy case, as far as practicable. Can the language of § 349 be interpreted to be so broad that a dismissal revokes an order of confirmation and/or revoke a debtor's discharge? Courts which have considered whether dismissal of a Chapter 11 case revokes a confirmed plan have consistently held that it does not. Such a case is In re Depew, 115 B.R. 965 (Bankr. N.D. Ind. 1989). "What § 349 does not say is as significant as what it says. If Congress had truly intended for dismissal to completely undo the bankruptcy, as though it had never existed, it would have been simple enough to have said so explicitly." In re Depew, 115 B.R. at 970-71. The Depew court, in explaining its conclusion that a confirmation order or the discharge that goes with it is unaffected by a post-confirmation dismissal stated that

> [i]t is confirmation of a Chapter 11 plan that discharges the debtor from its obligations . . . . For this reason revocation of the order of confirmation also requires revocation of the discharge. (citation omitted) Confirmation and discharge are inseparable events. Congress specifically recognized that dismissal would not vitiate a debtor's discharge. In view of the identity between the discharge and confirmation, Congress could not have intended for dismissal to vacate the order of confirmation which created a discharge that continues to be effective.

In re Depew, 115 B.R. at 970. See also, In re Bishop, 74 B.R. 677 (Bankr. M.D. Ga. 1987), In re Cronk, 124 B.R. 759 (Bankr. N.D. Ill. 1990), In re Mulberry Chesterton Inn, 142 B.R. 566 (Bankr. S.D. Ga. 1992), In re Space Building Corp., 206 B.R. 269 (D. Mass. 1996). Is the Internal Revenue Service without recourse in such a

situation?

The Service has taken the position that the debtor's default under a Chapter 11 plan entitles it to resume collection of discharged tax liabilities provided for by the plan. Furthermore, the Government is entitled to collect these liabilities not merely as contract rights created by the plan, but as tax liabilities subject to the administrative collection procedures of the Internal Revenue Code. See Matter of Official Committee of Unsecured Creditors of White Farm Equipment Company, 943 F. 2d 752 (7th Cir. 1991).

In summary, then, we conclude that the collection statute of limitations was suspended from the date of the partnership's filing of its Chapter 11 petition to the date of confirmation of its plan of reorganization and for six months thereafter. Because there is only one statute of limitation for collection applicable to this employment tax liability, the tolling of the statute with respect to the partnership also extended the period during which the Service could look to the partners for collection of that liability. The partnership's liability for the employment tax delinquency for the third quarter of [redacted] retains its character as a tax even after confirmation and dismissal of the Chapter 11 case and is collectible administratively.

Please call James Posedel of this office if there are any questions.

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CC: ARC (GL) ✓ KLF 1-20-99